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- Negotiations on joining the EU's Eastern Partnership.
- Exchange rate swap operation between NBB and People's Bank of China.
- A dramatic drop of exports to Russia.
- Further decrease of the international reserves.

Politics: Negotiations on joining the EU's Eastern Partnership

In February High Representative for the Common Foreign and Security Policy of the EU J. Solana came to Belarus with an official visit. During his meeting with the Belarusian President A. Lukashenko the issues of the cooperation between parties, and in particular, possible participation of Belarus in the EU program Eastern Partnership were discussed. Furthermore, it was stated that A. Lukashenko confirmed the readiness of Belarus to take part in the Eastern Partnership. No documents were signed after the meeting, but J. Solana expressed satisfaction with the results of his visit. Later, the minister of foreign affairs of the Czech Republic that is the current chair in the EU K. Schwarzenberg stated that if Belarus recognizes the independence of Abkhazia and South Osetia it will "be out of the European context" and it will embarrass its participation in the Eastern Partnership. A similar statement was done by the European Commissioner B. Ferrero-Walder, who also planned to visit Belarus in early March. But just before the visit it was postponed to April, which could suggest some growing contradictions between parties. However, later in March the EU Summit approved the Eastern Partnership program having included Belarus as its member, which might influence the long-term geopolitical priorities of Belarus.

Real sector: Deceleration of growth in 2009

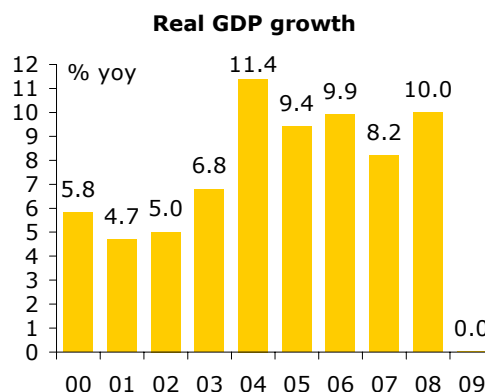
In January, real GDP grew by 4.2% yoy at the background of the economic recession in the neighboring countries. In Russia GDP dropped in January by 8.8% yoy, in Ukraine by more than 15%. However, Belarusian economic growth has been based on investment increase (financed by the government from 2008 funds) and consumption growth (caused by temporary hike in expenditures after devaluation). Both of these sources cannot sustain for the whole year, so one can expect growth deceleration February onwards.

Increase in inventories was another source of GDP increase (11.2% of the total industrial output in January). The problem is whether these inventories will be sold later, as Belarusian enterprises faces shrinking demand for their goods. In January merchandise exports in real terms dropped by 26.6% yoy, and domestic market can hardly substitute the external one.

Structural trends: Exchange rate swap operation between NBB and People's Bank of China

Since the beginning of the financial crisis Belarusian authorities declared the necessity of using national currencies in bilateral settlements with trade partners. In March the NBB informed about exchange rate swap with the People's Bank of China in national currencies, the volume of which is equivalent to the sum of about USD 2.9 bn. This transaction might be considered to be bilaterally beneficial. Belarus has a strong need in foreign currency for the stabilization of the domestic currency market and replenishment of the international reserves. From the Belarusian position this transaction might be considered as almost identical to direct borrowing. In its turn China might want to stimulate its exports to Belarus because

Population: 9.67 m
Industry / GDP: 28.1%
Agriculture / GDP: 8.4%
Investment / GDP: 27.9%
Export destination: Russia 32%, EU 44%
Import origin: Russia 60%, EU 22%



Source: Ministry of Statistics and Analysis. Forecast for 2008: IPM Research Center.

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of this transaction. It should be mentioned that problem of decreasing exports is the key one for China under the global crisis, while this sum of funds is not so substantial in the context of this country. Hence, China is likely to test a new mechanism of exports stimulation that may be later used with other countries.

NBB stated about launching measures directed at the de-dollarisation of the economy. The intention to de-dollarisation might be consequent to the deficit of the foreign currency at the domestic market during last months. Due to such measures NBB wants to increase the demand for the national currency, which dropped significantly in 2009. But it is unlikely that limitation of the spheres where the settlements in the foreign currency are allowed will result in substantial increase of the demand for the Belarusian ruble. Hence, trying to give an additional impulse to the de-dollarisation NBB recommended banks to reduce the interest rates on the foreign currency deposits. But the effectiveness of this measure seems to be also doubtful, while the direct regulation of the deposit market may cause a negative impact on the population behavior.

Foreign trade: A dramatic drop of exports to Russia

In 2008 the merchandise trade deficit amounted to USD 6.6 bn, having increased by 49.0% yoy (48.1% yoy in Jan-Nov). In 2008 exports grew by 35.5% yoy, while imports by 37.6% yoy. The growth of the trade volume was mainly driven by the price increase, which provided 95.3% of the exports growth and 61.2% of imports growth. Since the autumn of 2008 both average prices and physical volumes began to fall. In December, in comparison to September average prices of exports dropped by 41.1% in trade with non-CIS countries and by 11.8% in trade with Russia. The physical volume to the non-CIS countries grew in December by 4.1% yoy, while to Russia it dropped by 33.9% yoy.

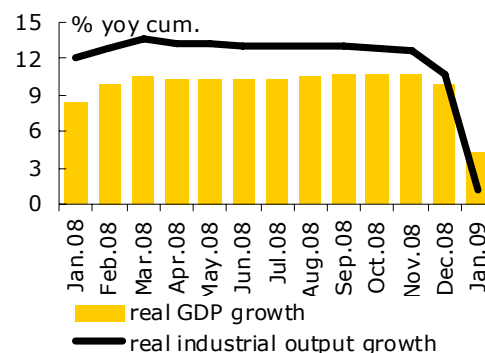
The supply of main goods to non-CIS countries – oil products and potash fertilizers – were touched by the global crisis through falling prices and hence exports (by 26.9% yoy in December). In trade with Russia the worst situation was with the supply of the investment goods. For instance, exports of tractors in December were about 50% of its monthly average volume in Jan-Sep, and trucks – 30.6%. The protection measures discussed in Russia may further worsen the stance of the Belarusian exporters of investment goods. Physical volumes of imports from Russia in December dropped only by 2.4% yoy, while the prices went down by 32.6% yoy. However, physical volume of imports from non-CIS countries kept on growing (by 5.8% yoy in December), while the prices decreased by only 1.3% yoy. This dynamics shows that Belarusian economic agents have not yet adjusted to the new economic conjuncture, keeping up the demand for both raw materials imports from Russia and consumer imports from the EU.

Public finance: Surplus of the consolidated budget

In 2008 consolidated revenues amounted to 51% of GDP, which is by 1.5 percentage points more than in 2007. This growth was due to higher revenues (by 1.8% percentage points of GDP) from taxes on external economic operations because of the high oil prices in Jan-Sep and from taxes on incomes and profit. At the same time, there was a decline of revenues from taxes on goods and services (because of the lower rate of the agricultural levy) and taxes on the wage fund, because the share of wages in GDP decreased in 2008.

Consolidated expenditures in 2008 amounted to 49.5% of GDP, which is by 0.6 percentage points more than in 2007. The growth was provided by the drastic increase of the gov

GDP and Industrial Output



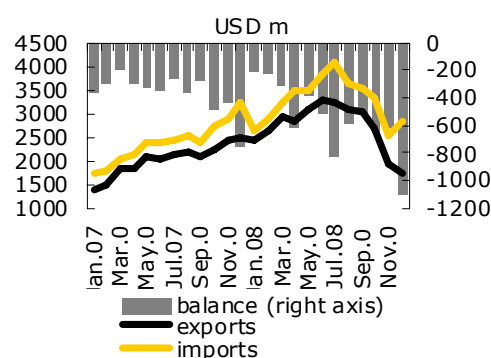
Source: National Statistical Committee.

Contribution to Industrial Output Growth

January 2009	Growth	
	%	Contribution*
Industry, total	-0.3	-0.3
Electric power	-10.6	-0.8
Fuel	6.4	1.5
Ferrous metallurgy	4.5	0.2
Chemical and petrochemical industry	29.6	3.2
Machinery and metalworking	-21.7	-4.5
Logging, woodworking, pulp and paper	-21.0	-0.6
Building materials	-21.6	-0.6
Light	-18.9	-0.6
Food	5.5	0.6
Other	8.6	1.1

Note. * - data is given in percentage points.
Source: National Statistical Committee.

Merchandise Trade



Source: National Statistical Committee.

ernment investments, which led to the increase of the "state expenditure" by 1.7 percentage point of GDP. Moreover, the expenditures "on the economy" and housing and utilities infrastructure was increased as well. Other items of the budget performed decreasing expenditure: social policy by 0.8, education by 0.5 and healthcare by 0.5 percentage points of GDP. This change in expenditure structure witnesses the change in priorities of the budget policy, which might express in substantial decrease of the social expenditure in 2009.

Monetary policy: Drop of the international reserves

In January, net foreign assets of the monetary authorities dropped by 11.4% mom (by USD 364.4 m). However without the first tranche of the IMF loan, net foreign assets would have dropped by 36% mom (USD 1.15 bn). The NBB tried to bound demand for hard currency, having increased the refinancing rate by 2 percentage points up to 14% and correspondingly other rates on the NBB operations. However, at the same time the NBB trying to stimulate domestic credit market increased the volume of resources for refinancing of banks and claims on banks increased by 45.5% mom. Finally, base money in January decreased by 28.0% mom, while in annual terms it decreased by 9.3% yoy.

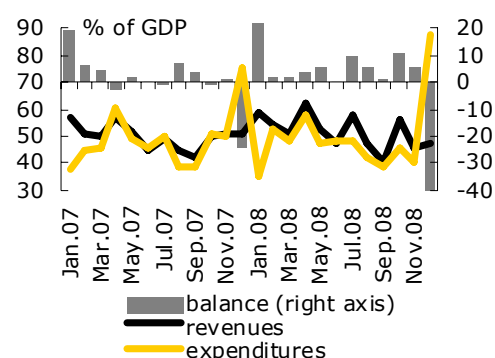
In this situation claims of banks on the economy grew by 6.5% mom, while in annual terms its growth rate amounted to 64.1% yoy (54.9% yoy in December), but without re-estimation of the claims in foreign currency it was 52.5% yoy. Interest rates at the interbank market and also at the credit and deposit market grew substantially on both national and foreign currency contracts. This allowed avoiding huge net outflow of saving by population from the banking system. In January, households withdraw about 13.8% of ruble deposits, but nearly all these funds were re-deposited in banks in hard currency – households' deposits in foreign currency grew by 10.3% mom (about 38.0% mom in ruble equivalent). However, net outflow of the legal entities' deposits was more significant, which alongside with decreased demand for cash money (by 18.1% mom) exerted a pressure for the domestic money market. Finally ruble money decreased in January by 18.4% mom, while broad money by 2.4%. In annual terms its growth rates amounted to 11.3 and 32.0% yoy (28.0 and 30.2% yoy in December).

Consumer prices in January grew by 4.1% mom and in annual terms inflation amounted to 15.1% yoy (13.3% yoy in December). The Belarusian ruble was devaluated through January by 25.1% and later in February by additional 3.9%. As of February 28, its exchange rate was 2858 USD/BYR.

Banking sector: Argues about collector agencies

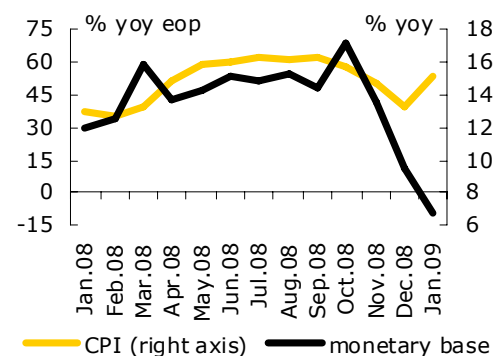
NBB declared its intention to launch a legislative base in Belarus for a legal activity of the collector agencies, which are rather wide-spread in other countries. The discussion on the necessity of establishment of the collector agencies was initiated by the NBB because of the increasing non-performing loans in the banking system under the condition of the financial crisis. They hope that this kind of the specialized institutions will contribute to the reduction of the overdue credit indebtedness. However, current Belarusian legislation allows debt assignment only for banks, while collector activity cannot be the main one. Furthermore, the experience of the neighboring countries shows that the activity of the collector agencies may contradict to the principle of the bank secret and thus lead to social protests. Thus, on the one hand, it may lead to higher financial discipline by borrowers, but on the other hand it may decrease propensity to borrow at least by physical entities and cause negative social consequences.

Consolidated Budget



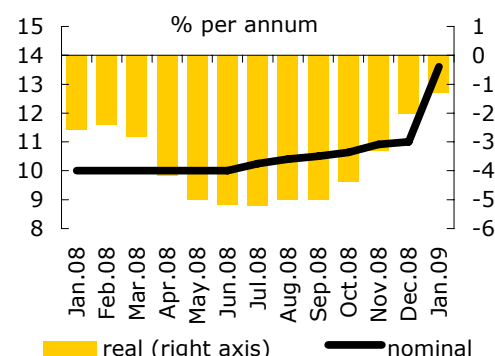
Source: calculations based on the National Statistical Committee data.

Monetary Base and CPI



Source: calculations based on the National Statistical Committee and the NBB data.

Refinancing rate



Source: calculations based on National Statistical Committee and the NBB data.

Economic Trends		Q1 07	Q2 07	Q3 07	Q4 07	Q1 08	Q2 08	Q3 08	Q4 08	Nov. 08	Dec 08	Jan 09
GDP growth	% yoy	8.4	8.9	8.4	7.3	10.9	10.1	11.2	7.5			
GDP growth	% yoy cum.	8.4	8.6	8.4	8.2	10.9	10.4	10.7	10.0	10.8	10.0	4.2
Industrial Production	% yoy cum.	5.9	7.7	8.2	8.5	14.7	13.0	13.1	10.8	12.7	10.8	1.2
Agricultural Production	% yoy cum.	4.4	5.2	5.6	4.1	6.8	5.4	6.9	8.9	8.9	8.9	8.4
CPI	% yoy eop	8.1	7.2	9.0	12.1	13.2	16.0	16.3	13.3	14.7	13.3	15.1
PPI	% yoy eop	11.6	13.6	16.8	17.1	13.5	16.2	18.5	14.2	18.2	14.2	19.9
Merchandise export (USD)*	% yoy	6.3	23.3	18.5	44.4	69.2	56.0	44.9	-11.6	-19.1	-29.8	--
Merchandise import (USD)*	% yoy	20.8	23.7	23.8	42.4	56.5	55.3	53.1	-1.5	-11.4	-12.2	--
Merchandise trade balance (NBB data)	USD m cum.	-836	-1563	-2304	-3858	-647	-2049	-3835	-6104	-5059	-6104	--
Current account	USD m cum.	-641	-1152	-1652	-2944	-433	-1411	-2920	-5049	--	-5049	--
Current account	% GDP cum	-7.0	-5.8	-5.1	-6.6	-3.6	-5.5	-6.6	-8.0	--	-8.0	--
International reserves	USD m eop	1565	2344	2155	4182	4746	4618	4120	3061	3775	3061	2929
Monetary base	% yoy eop	22	29	25	38	59	54	48	12	42	12	-9
Lending rate**	% p.a. aop	14	11	12	12	11	10	11	14	14	15	20
Exchange rate (official)	USD aop	2141	2145	2147	2152	2148	2136	2114	2147	2137	2190	2668
Exchange rate (official)	EUR aop	2805	2890	2948	3115	3215	3339	3183	2827	2719	2935	3544

* Growth rates in value terms (source: Ministry of Statistics and Analysis).

** Nominal rate of commercial banks for new loans for legal entities in national currency.

Sources: Ministry of Statistics and Analysis, NBB.

Key Economic Indicators		2002	2003	2004	2005	2006	2007	2008
Nominal GDP*	BYR trn	26.613	36.565	49.991	65.067	79.231	96.047	128.828
Nominal GDP**	USD bn	14.5	17.7	23.1	30.2	36.9	44.8	60.3
GDP Growth	% yoy	5.0	7.0	11.4	9.4	9.9	8.6	10.0
Industrial production	% yoy	4.5	7.1	15.9	10.5	11.3	8.7	10.8
Agricultural production	% yoy	0.7	6.6	12.6	1.7	6.1	4.4	8.9
CPI	% yoy aop	42.6	28.4	18.1	10.3	7.0	8.4	14.8
CPI	% yoy eop	34.8	25.4	14.4	8.0	6.6	12.1	13.3
PPI	% yoy aop	41.4	37.5	24.1	12.1	8.3	16.2	15.6
PPI	% yoy eop	42.7	28.1	18.8	10.0	8.5	17.1	14.2
Exports (gs, USD)	% yoy	9.8	24.4	35.5	15.9	22.3	24.0	35.5
Imports (gs, USD)	% yoy	9.0	25.0	40.4	3.8	33.2	28.0	37.6
Current account	USD m	-334	-426	-1193	436	-1448	-3060	-5049
Current account	% GDP	-2.3	-2.4	-5.2	1.4	-3.9	-6.8	-8.0
FDI (net)	USD m	453	170	163	303	351	1770	2143
International reserves	USD m	457	474	770	1297	1383	4182	3467
Fiscal balance	% GDP	-0.2	-1.6	0.0	-0.6	2.2	0.6	0.9
Domestic public debt	% GDP eop	5.4	5.5	5.7	5.8	6.5	6.4	6.7
External debt (total)	% GDP eop	27.0	23.7	21.4	17.9	18.6	28.4	24.6
Monetary base	% yoy eop	32	50	42	74	20	38	12
Exchange rate (official)*	USD aop	1784	2075	2160	2154	2145	2146	2136
Exchange rate (official)*	USD eop	1920	2156	2170	2152	2140	2150	2200
Exchange rate (official)*	EUR aop	1690	2353	2684	2681	2692	2937	3135
Exchange rate (official)*	EUR eop	1989	2695	2956	2550	2817	3167	3077

* On January 1, 2000 the Belarusian ruble was denominated 1:1000. All figures for 1999 are given in 'new' Belarusian rubles.

** For the period of 1999–2000, GDP in USD is calculated by using the market (unofficial) exchange rate (source: IPM Research Center).

Sources: National Statistical Committee, Ministry of Finance, NBB, IPM Research Center.

Notes:

aop	average of period	gs	goods and services
avg	average	trn	trillion
bn	Billion	NBB	National Bank of Belarus
cum.	cumulative	p.a.	per annum
eop	end of period	yoy	year-on-year
m	million	ytd	year-to-date